No. 91-918

In The Supreme Court Of The United States

OCTOBER TERM, 1991

JOHN R. PATTERSON, TRUSTEE,

Petitioner,

v.

JOSEPH B. SHUMATE, JR.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Is the antialienation requirement of 29 USC §1056(d)(1) included as "applicable nonbankruptcy law" under 11 USC §541(c)(2) or is "applicable nonbankruptcy law" limited to state spendthrift trust law?

2. Does the ERISA antialienation provision of 29 USC §1056(d)(1) qualify a bankruptcy debtor's interest in a qualified retirement plan as "property exempt under Federal law" under 11 USC §522(b)(2)?

3. If the antialienation provisions of 29 USC §1056(d)(1) either create a federal exemption under 11 USC §522(b)(2) or qualify as "applicable nonbankruptcy law" under 11 USC 541(c)(2), is there an enforceable public policy barring a debtor in bankruptcy from sheltering his interest in an ERISA qualified retirement plan over

which the debtor held significant dominion, control and revocation power?

11 USC §541(a)(1) of the Bankruptcy Code creates an estate of "all legal or equitable interests of the debtor" but excludes the debtor's interest in a trust which is subject to an enforceable restriction on its transfer under "applicable nonbankruptcy law" in 11 USC §541(c)(2). 11 USC §522(b)(2) of the Bankruptcy Code authorizes an exemption from the bankruptcy estate of "any property that is exempt under federal law." The Employment Retirement Income Security Act (ERISA), through 29 USC §1056(d)(1), requires all qualified retirement plans to contain an antialienation provision in the plan's trust agreement. Respondent was a participant in a qualified retirement plan, containing the antialienation provision required by ERISA, but he had the power to

terminate the plan at will and receive his plan interest free of the trust. The Courts of Appeal are in conflict as to whether ERISA excludes (or exempts) such an interest in a qualified retirement plan from a debtor's estate in bankruptcy.

LIST OF PARTIES

The parties are the Petitioner, John R. Patterson, Trustee in Bankruptcy for Joseph B. Shumate, Jr., and the Respondent, Joseph B. Shumate, Jr.

In the District Court proceedings, Roy V. Creasy, Trustee in Bankruptcy for Coleman Furniture Corporation; Roy V. Creasy, Trustee and Plan Administrator of the Coleman Furniture Corporation Pension Plan; William Mercer Meidinger and NCNB Financial Services, Inc. were named parties. None of these parties has an interest in the outcome of this proceeding, none participated in the case below in the Court of Appeals, and therefore, none are named as parties herein.

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JOHN R. PATTERSON, TRUSTEE, *Petitioner*,

v.

JOSEPH B. SHUMATE, JR., *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Petitioner, John R. Patterson, Trustee, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit, entered in the above entitled proceeding on August 12, 1991.

OPINIONS BELOW

The opinion of the Court of Appeals for the Fourth Circuit is reported at 943 F.2d 362, and is reprinted in the appendix hereto, p. 1a, infra.

The decision of the United States District Court for the Western District of Virginia is reported at 83 B.R. 404, and is reprinted in the appendix hereto, p. 18a, infra. The District Court also issued a Memorandum Opinion dated April 13, 1988, which has not been reported, but is reprinted in the appendix hereto, p. 47a, infra, and a Final Order on September 1, 1988, which is reprinted in the appendix hereto, p. 52a, infra.

JURISDICTION

The United States District Court for

the Western District of Virginia entered its decision March 1, 1988, with a Final Order on September 1, 1988, holding Respondent must turnover his pension interest to the Petitioner, his bankruptcy Trustee. See p. 18a, infra and 52a, infra.

Respondent appealed to the Court of Appeals for the Fourth Circuit which reversed the District Court in an opinion entered August 12, 1991. See p. 1a, infra. No petition for rehearing was sought, but the Fourth Circuit stayed its Mandate pending appeal to this Court by Order entered September 13, 1991. See p. 58a, infra.

The jurisdiction of this Court to review the judgment of the Fourth Circuit Court of Appeals is invoked under 28 USC §1254(1).

STATUTES INVOLVED

1. 11 USC §522(b)(2)(A), reprinted in the appendix hereto, p. 60a, infra;

2. 11 USC §541(c)(2), reprinted in the appendix hereto, p. 61a, infra;

3. 26 USC §401(a)(13)(A), reprinted in the appendix hereto, p. 62a, infra;

4. 29 USC §1056(d)(1), reprinted in the appendix hereto, p. 63a, infra; and

5. 29 USC §1144(d), reprinted in the appendix hereto, p. 64a, infra.

STATEMENT OF THE CASE

Coleman Furniture Corporation (hereinafter CFC) filed for bankruptcy under Chapter 11 of the Bankruptcy Code in November, 1982. Roy V. Creasy (hereinafter Creasy) was appointed Bankruptcy Trustee for CFC in February, 1983, when CFC's case

was converted to a Chapter 7 proceeding. In addition to his duties as Trustee in Bankruptcy for CFC, Creasy was appointed Plan Administrator of the Coleman Furniture Corporation Pension Plan (hereinafter CFC Plan). CFC established the CFC Plan in 1963 and maintained it as a qualified retirement plan under the Internal Revenue Code. The CFC Plan contained the antialienation clause required by 26 USC §401(a)(13)(A) and 29 USC §1056(d)(1).

Creasy brought an action in the United States District Court for the Western District of Virginia culminating in Court approval to terminate the CFC Plan. See Creasy v. Coleman Furniture Corporation, 763 F.2d 656 (4th Cir. 1985).

Of approximately 400 CFC Plan participants, all except Joseph B. Shumate, Jr., the Respondent (hereinafter Shumate), received their account benefits in

termination distributions from Creasy. The CFC Plan, upon satisfying payments to all plan participants, had a surplus which is a reversion payable to CFC.

Shumate filed for Chapter 11 bankruptcy protection on June 1, 1984, and was converted to a Chapter 7 proceeding on August 24, 1984. John R. Patterson, Trustee, the Petitioner (hereinafter the Trustee), was then appointed Shumate's Trustee in bankruptcy.

The Trustee, pursuant to 11 USC §542, filed an Adversary Proceeding in the United States Bankruptcy Court on April 24, 1987, for the turnover of Shumate's CFC Plan benefit to his bankruptcy estate. Shumate responded by filing a motion, invoking jurisdiction under 29 USC §1132 in an existing District Court civil action concerning the CFC Plan, to compel Creasy to pay the CFC Plan benefits over to him.

The Trustee intervened in the District Court action, into which the Adversary Proceeding was consolidated, and all matters relating to Shumate's CFC Plan interest were heard in that proceeding.

Shumate was Chairman of the Board of Directors, corporate President, and the majority shareholder of CFC from 1978 through at least February, 1983. Shumate has owned and controlled at least 96% of the issued and outstanding CFC stock from 1979 to the present as majority stockholder. Jt. Ap. Vol. I, p. 109, 110.

As CFC's majority stockholder, Shumate could replace the CFC Board of Directors at will. Jt. Ap. Vol. I, p. 131. The CFC Board of Directors could terminate the CFC Plan at will without cause. Jt. Ap. Vol. II, p. 290. The District Court found "therefore, Shumate could have terminated the plan at any time before the bankruptcy

and received not only his pension interest, but any excess funds not needed to satisfy the rights of other participants." See p. 23a, infra. Shumate "could have paid himself the reversion of any overfunded amount as a dividend on his stock." See p. 37a, infra.

Shumate, Creasy, and the Trustee entered into an Agreement and Agreed Order dated December 3, 1987, fixing Shumate's CFC Plan interest at $250,000.00. Jt. Ap. Vol. I, pp. 90-96. Under this Agreed Order, Creasy paid the $250,000.00 to the Clerk of the United States District Court for the Western District of Virginia, to be held in an interest bearing account.

The Trustee argued at trial that the CFC Plan interest was property of the bankruptcy estate under the broad reach of 11 USC §541(a): "all legal and equitable interest of the debtor in property." The

chief task for the District Court was to determine if Shumate could exclude that interest from property of the estate under the argument that the CFC Plan's alienation provision was an applicable nonbankruptcy law restriction on transfer under 11 USC §541(c)(2). If not, unless an exemption could be found under 11 USC §522(b), then the CFC Plan interest must be turned over to the Trustee. See p. 25(a), infra.

Citing the Fourth Circuit's decision in McLean v. Central States Pension Fund, 762F.2d 1204 (4th Cir.1985), as authority, the District Court Judge ruled that the Fourth Circuit had interpreted "applicable nonbankruptcy law" to mean state law. See p. 26a, infra, citing McLean, 762 F.2d at 1206, 1207. The District Court then reviewed Virginia spendthrift trust law and found spendthrift trusts are invalidated where a debtor exercises such control over

the trust as to (in effect) be both settlor and beneficiary by virtue of the power to terminate the trust. See p. 35a, infra.

Due to Shumate's pervasive control and revocation power over the CFC Plan and his interest in it, he was in effect settlor and beneficiary. Accordingly, the District Court held the pension interest was not excluded from Shumate's bankruptcy estate. Virginia public policy invalidated spendthrift trust protection in such circumstances.

The District Court also determined that the antialienation clause in the CFC Plan required by 29 USC §1056(d)(1) did not protect Shumate's interest as "exempt under federal law" within the context of the applicable Bankruptcy Code exemption provision, 11 USC §522(b)(2). Finding Virginia had opted out of the Bankruptcy Code's exemption scheme, the District Court

followed a line of Court of Appeals decisions holding ERISA was not intended by Congress to be a "federal exemption" under 11 USC §522(b)(2). See p. 44a, infra.

The Fourth Circuit, by a decision dated August 12, 1991, held that "applicable nonbankruptcy law" under 11 USC §541(c)(2) does include ERISA and reversed the District Court decision. Citing Anderson v. Raine (In Re Moore), 907 F.2d. 1476 (1990) as authority, the Court of Appeals ruled that the antialienation language required by 29 USC §1056(d)(1) is "applicable nonbankruptcy law" which acted to exclude Shumate's pension interest from his bankruptcy estate. In the Fourth Circuit's view, there was no public policy restriction permitted by ERISA regardless of the degree of control a debtor may have over his retirement plan interest. See p. 11a, infra. Having found the controlling

application of ERISA as applicable nonbankruptcy law under 11 USC §541(c)(2), the Fourth Circuit did not reach the 11 USC §522(b)(2)(A) exemption question. See p. 16a, infra.

REASONS FOR GRANTING THE WRIT

The Fourth Circuit's decision that "applicable nonbankruptcy law" includes ERISA, and is not limited to state spendthrift trust law, directly conflicts with many decisions of other Courts of Appeals, the legislative history of the Bankruptcy Code and public policy. An ancillary ground of decision deeming ERISA to create a federal exemption in bankruptcy also conflicts with

other Court of Appeals decisions, the legislative history of the Bankruptcy Code and public policy.

The crux of this case is whether a debtor in bankruptcy, who can control and cause the termination of his interest in a qualified retirement plan, can seek bankruptcy protection and avoid turnover of that interest to the trustee. The precise conflict lies in differing interpretations of the requirements of the Bankruptcy Code and ERISA. A multitude of Courts of Appeal, District Court and Bankruptcy Court decisions are in direct conflict over the questions represented by this case.

The Bankruptcy Code, by 11 USC §541(a), creates a bankruptcy estate of "all legal or equitable interests of the debtor in property" to be turned over to

the debtor's trustee for distribution to creditors. ERISA, by 29 USC §1056(d)(1), requires that "each pension plan shall provide that benefits provided under the plan may not be assigned or alienated". A similar provision is included in the Internal Revenue Code, 26 USC §401(a)(13)(A), relating to tax qualification for retirement plans.

Debtors, like the Respondent, argue such an antialienation provision contained in an ERISA qualified plan creates a restriction on transfer enforceable under "applicable nonbankruptcy law" under 11 USC §542(c)(2) so as to exclude the retirement interest as property of the bankruptcy estate. Debtors also contend the antialienation provision creates a federal law exemption under 11 USC §522(b)(2)(A) exempting a qualified retirement plan interest from the grasp of the bankruptcy

trustee.

Bankruptcy trustees, like the Petitioner, contend the Bankruptcy Code prevails over any apparent conflict with ERISA to include retirement interests as estate property. This argument is buttressed by the legislative history of the Bankruptcy Code which displays the intent of Congress that the phrase "applicable nonbankruptcy law" in 11 USC §541(c)(2) means only state spendthrift trust law. The legislative history and rules of statutory construction undergird the proposition that ERISA does not create an ERISA exclusion from the bankruptcy estate as to do so would render the Bankruptcy Code's exemption scheme in 11 USC §522(b) and (d) unnecessary and useless. The Courts of Appeal which affirm the Petitioner's viewpoint note the primacy of the Bankruptcy Code to include a

debtor's plan benefit in the estate under 11 USC §541(a) over any conflicting ERISA provision as 29 USC §1144(d) provides that ERISA does not modify or supersede other federal law.

I. Applicable nonbankruptcy law in 11 USC §541(c)(2) refers to state spendthrift trust law and was not intended by Congress to include ERISA.

The apparent conflict between the Bankruptcy and ERISA statutory directives has split the Courts of Appeal. Four Circuits have ruled that the Bankruptcy Code prevails and found through the legislative history of the Bankruptcy Code, that "applicable nonbankruptcy law" in 11 USC §541(c)(2) is meant to refer to state spendthrift trust law, and not other statutory enactments such as ERISA. Daniel v. Security Pacific National Bank,

771 F.2d. 1352 (9th Cir. 1985), cert. den. 106 S.Ct. 1199; Goff v. Taylor, 706 F.2d. 574 (5th Cir. 1983); Lichstrahl v. Banker's Trust, 750 F.2d. 1488 (11th Cir. 1985); Samore v. Graham, 726 F.2d. 1268 (8th Cir. 1985).

These four Courts of Appeal examined the legislative history of the Bankruptcy Code to conclude "Congress intended its reference to applicable nonbankruptcy law to exempt from the estate only those spendthrift trusts traditionally beyond the reach of creditors under state law." Goff, 706 F.2d at 582 and citing S. Rep. No. 95-989, 95th Cong., 2d Sess. 83, reprinted in 1978 U.S. Code Cong. and Ad. News 5787, 5869. This evidence of Congressional intent to limit exclusions from the bankruptcy estate is confirmed by the specific inclusion of ERISA benefits in the Bankruptcy Code's exemption provision, 11

USC §522(d)(10)(E). These Courts of Appeal reasoned that Congress would not have specifically dealt with ERISA benefits as an exemption from the bankruptcy estate in 11 USC §522 if it had intended the 11 USC §541(c)(2) provision to create an ERISA exclusion thereby rendering the exemption provision superfluous. As the Fifth Circuit noted in Goff:

> We find that Congress did not intend to do ambiguously in Section 541 that which it clearly did not do directly in Section 522, although Section 522 explicitly addresses the extent to which other "Federal law" and retirement benefit exemptions would be recognized. 706 F.2d at 582.

Even the most scholarly opinion holding ERISA creates an omnibus federal exemption under 11 USC §522(b)(2)(A), accepts the proposition that 11 USC §541(c)(2) does not include ERISA as "applicable nonbankruptcy law." In Re

Komet, 104 B.R. 799, 816 (W.D. Texas, 1989).

Accordingly, in the Fifth, Eighth, Ninth and Eleventh Circuits, a debtor's qualified retirement benefit is included as property of the bankruptcy estate under 11 USC §541(a) with the matter of whether some or all of the Debtor's interest is exempt being determined under 11 USC §522.

The Fourth Circuit broke with the other Courts of Appeal in Anderson v. Raine, (In Re Moore), 907 F.2d 1476 (4th Cir. 1990), holding that ERISA prevailed over any perceived conflict with the Bankruptcy Code in that "applicable bankruptcy law" under 11 USC §541(c)(2) did include ERISA and was not restricted to state spendthrift trust law. Accordingly, a debtor's interest in a qualified retirement plan was to be excluded from the bankruptcy estate on the grounds that the

plan's antialienation provision (required by ERISA) was an effective restriction on transfer under 11 USC §541(c)(2).

Although the Fourth Circuit apparently adopted the Goff line of cases, interpreting 11 USC §541(c)(2) to mean state law, in McLean v. Central States Pension Fund, 762 F.2d 1204 at 1206, the Anderson court chartered a different course discounting the conclusions from the Bankruptcy Code's legislative history drawn by the other Courts of Appeal.

> "Applicable nonbankruptcy law" means precisely what it says: all laws, state and federal, under which a transfer restriction is enforceable. Nothing in the phrase "applicable nonbankruptcy law" or in the remainder of 541(C)(2) suggests that the phrase refers exclusively to state law, much less to state spendthrift trust law." 907 F.2d at 1477.

No appeal was taken from the Anderson v. Raine decision.

The Sixth Circuit Court of Appeals adopted the viewpoint of the Fourth Circuit in its decision In Re Lucas, 924 F.2d 597 (6th Cir. 1991). An appeal was taken but certiorari was denied. 111 S.Ct. 2275.

The Fourth Circuit followed its Anderson principle in the case at bar to hold that Shumate's CFC Plan interest was excluded from his bankruptcy estate under 11 USC §541(c)(2). The Court of Appeals held the ERISA required antialienation provision in the CFC Plan restricted the plan interest as "applicable nonbankruptcy law" so as to exclude it from Shumate's bankruptcy estate. In the Fourth Circuit's view, this is the case regardless of the control, including the power to terminate, held by the debtor over his qualified plan interest. See p. 12a, infra.

The debtors in Anderson and Lucas had no control over the retirement plan in

which each was a participant. They were basically rank and file workers with no ability to terminate their plan interest. By contrast, Shumate as majority stockholder, director and corporate president, could direct at any time that the CFC Plan be terminated and thereupon receive his plan interest and the value of the plan reversion to CFC free of any trust. This power of revocation under Virginia law, as interpreted by the District Court, vitiates the protection of the antialienation provision of the CFC Plan, as to Shumate, since that power essentially makes Shumate settlor and beneficiary of his trust.

The Fourth Circuit did not address the argument that finding a comprehensive ERISA exclusion from the bankruptcy estate by deeming ERISA to be "applicable nonbankruptcy law" under 11 USC §541(c)(2)

is inconsistent with the treatment of ERISA benefits as an exemption under 11 USC §522(b)(2) (thereby rendering 11 USC §522(d)10)(E) unnecessary). Similarly, the Fourth Circuit did not address the argument that ERISA's noninterference with other federal law provision (29 USC §1144(d) gives the Bankruptcy Code's definition of property of the estate pre-emption over any derivative ERISA protection based on the CFC Plan's restriction on transfer.

The result of the Anderson and Shumate decisions places debtors, bankruptcy trustees, and qualified retirement plans in irreconcilable and conflicting positions depending upon the state or even district of residence. In some districts a debtor's control over his retirement benefits, no matter how great, permits him to exclude those assets from the reach of his bankruptcy trustee. Yet in a neighboring

district, a similarly situated debtor must surrender this asset to the Trustee for the benefit of his creditors. Had the Shumate case arisen in the Fifth, Eighth, Ninth or Eleventh Circuits, the CFC Plan interest would have been directed to the Petitioner as Trustee.

Thousands of bankruptcy trustees, debtors, and the fiduciaries and beneficiaries of retirement plans are now subject to conflicting rules, persistent litigation and unknown fiduciary liability with the results on the same facts absolutely contrary from one district to another. The multitude of litigation is vast.

In the Fourth Circuit, a bankruptcy trustee who now litigates the turnover of a debtor's retirement plan interest could be subject to sanctions under Rule 11 while an identically situated trustee in the

Fifth Circuit may be surcharged for violating his fiduciary duty if he <u>fails</u> to litigate the turnover of an identical debtor's retirement plan interest. Similarly, the fiduciary of a retirement plan must now treat the interest of identical debtor/participants' plan interests differently and at great risk. The plan fiduciary who pays over a debtor's plan interest to a bankruptcy trustee in the Fourth Circuit could be subject to a personal surcharge for so doing, while the same fiduciary of the same plan in the Fifth Circuit could be in contempt of Court or surcharged if he <u>failed</u> to pay over the debtor's interest to the bankruptcy trustee.

Any beneficiary of a qualified retirement plan who contemplates bankruptcy is well advised to change legal residence to a district following the <u>Shumate</u>,

Anderson and Lucas cases. While some forum shopping by debtors looking for more favorable state exemptions occurs, in the area of retirement benefits the cause is solely the inconsistency of federal law from district to district.

The Fourth Circuit's decision that ERISA is "applicable nonbankruptcy law" under 11 USC §541(c)(2) which restricts the transfer of Shumate's CFC Plan interest should be reversed. Congress intended to restrict "applicable bankruptcy law" to state spendthrift trust law and crafted a careful exemption scheme in 11 USC §522 to cover retirement benefits. The Shumate decision erroneously ignores the legislative history of 11 USC §541(c)(2) and violates the rules of statutory construction by rendering 11 USC §522(d)(10)(E) superfluous.

II. ERISA does not create a federal exemption in bankruptcy under 11 USC §522(b)(2)(A).

Should the Supreme Court reverse the Fourth Circuit's decision below by determining its interpretation of "applicable nonbankruptcy law" in 11 USC §541(c)(2) was incorrect, the dilemma of Bankruptcy trustees, debtors and retirement plan fiduciaries and beneficiaries would be little ameliorated without also determining whether ERISA creates an omnibus federal bankruptcy exemption under 11 USC §522(b)(2)(A). While the Fourth Circuit in this case did not feel the need to reach this question, see p. 16a, infra, the Fifth, Eighth, Ninth and Eleventh Circuits all addressed this issue in their opinions, to which other courts disagree and hold to the contrary. See Komet, supra.

The Fifth, Eighth, Ninth and Eleventh

Circuits concluded ERISA was not a "federal exemption" under 11 USC §522(b)(2)(A), but that such exemptions were limited to federal government program benefits which by specific statutory directive were exempt from any seizure. See Daniel 771 F.2d at 1361. This determination was based in part on the statutory interlock of the varying exemption schemes in 11 USC §522 as well as the legislative history of 11 USC §522 which did not include ERISA in a long listing of specific federal exemption statutes. See S. Rep. No. 989, 95th Cong. 2d Sess. 75 reprinted in 1978 U.S. Code Cong. & Ad. News 5787, 5861.

11 USC §522 permits each state to choose whether debtors are limited to only those exemptions in bankruptcy permitted by that state (commonly termed "opt out") or, may use the Bankruptcy Code exemptions set out in 11 USC §522(d). Under 11 USC

§522(d)(10)(E), a debtor in a state permitting the Bankruptcy Code exemptions is entitled to exempt from the bankruptcy estate his ERISA qualified plan benefits, but only "to the extent reasonably necessary for the support of the debtor..."

Virginia, the applicable state for Shumate, "opted out" of the Bankruptcy Code exemption scheme and thus limits debtors to Virginia exemptions in bankruptcy under 11 USC §522(b)(2) and whatever comprises federal exemptions other than those exemptions appearing in 11 USC §522(d). The Daniel, Goff, Lichstrahl and Graham Courts found the specific exemption for pension benefits in 11 USC §522(d)(10)(E) to reflect that Congress could not have intended a comprehensive ERISA exemption for such benefits under 11 USC §522 (b)(2)(A). To do so would render the 11 USC §522(d)(10)(E) exemption superfluous as

well as incongruous. How could ERISA be deemed to create a comprehensive "federal exemption" through 29 USC §1056(d)(1) in "opt out" states like Virginia under 11 USC §522(b)(2)(A) (which would shelter all of Shumate's benefits), but yet have debtors limited to a lesser amount in other states (using the Bankruptcy Code exemptions) to "the extent reasonably necessary for the support of the debtor under 11 USC §522(d)(10)(E)?" 706 F. 2d at 585; 771 F. 2d at 1361.

As the Fifth Circuit concluded in Goff, after examining the legislative history of 11 USC §522, the "federal exemptions" intended by that statute were those with a direct statutory prohibition on alienation such as for Civil Service Retirement benefits. 706 F.2d at 583.

> The money mentioned by this subchapter is not assignable, either in law or equity ... or

> subject to execution, levy, attachment, garnishment, or other legal process. 5 USC §8346.

ERISA, by contrast in 29 USC §1056(d)(1), does not provide a direct statutory prohibition on alienation, but instead directs the plan trust to include a protective provision. The Fifth Circuit has interpreted this method not to give a debtor's retirement benefits derivative protection under ERISA.

> "If Congress had intended that ERISA would provide such an exemption, a provision similar to 5 USC §8346 would have been enacted." 706 F.2d at 574.

In this case, the District Court confirmed Virginia was an "opt out" state so the specific ERISA exemption of 11 USC §522(d)(10)(E) was unavailable to Shumate. Citing Goff, Lichstrahl, Graham and Daniel, the District Court held that the Bankruptcy Code's legislative history did not support

including ERISA as a federal exemption under 11 USC §522(b)(2). Accordingly, Shumate's CFC Plan interest was not exempt property. See p. 45a, infra.

The Supreme Court should adopt the reasoning of the Courts of Appeal which hold that ERISA does not create a "federal law" exemption under 11 USC §522(b)(2)(A), and that exemption of ERISA plan benefits in bankruptcy is determined by state law in "opt out" states and by 11 USC §522(d)(10)(E) in other states. If this Court concurs with the Petitioner to reverse the Fourth Circuit's ruling that "applicable nonbankruptcy law" includes ERISA under 11 USC §541(c)(2), the current conflict between districts would be virtually unaffected unless the federal exemption question under 11 USC §522(b)(2) is also determined.

III. *Longstanding public policy prohibits a bankruptcy debtor with dominion, control and the right to terminate the retirement plan in which he has an interest, from sheltering that asset from his bankruptcy estate.*

In McLean, supra, the Fourth Circuit appeared to endorse the proposition that regardless of whether an ERISA exclusion under 11 USC §541(c)(2) or an exemption under 11 USC §522 could be found, there was an overriding public policy found in state law which could void the antialienation protection of a debtor's retirement interest.

> The pension fund is not one of those which because settled and revocable by a beneficiary, may not on that account for public policy reasons be protected against the claims of the beneficiary's creditors by antiassignment provisions. 762 F.2d at 1204.

The District Court below relied

heavily on this public policy, citing McLean, that a trust beneficiary with control so as to revoke a trust at will and receive the assets would not be protected from his creditors. See p. 29a infra. Shumate was found to have that type of all pervasive control which Virginia spendthrift trust law would not protect. In such cases, the District Court determined, "Public policy demands that debtors not be allowed access to their funds to the detriment of creditors." See p. 36a, infra. Accord, Richardson v. TIAA/CREF, 123 B.R. 540 (E.D.N.C.1991).

Even if the Court determines ERISA is "applicable nonbankruptcy law" under 11 USC §541(c)(2) or a federal exemption in bankruptcy under 11 USC §522(b)(2), it should still reverse the Fourth Circuit's decision to preserve the fundamental public policy against self-settled trusts acting

to thwart creditors in bankruptcy. Otherwise, debtors like Shumate can set up retirement funds directly or indirectly which they can drain of assets, to the exclusion of creditors, once bankruptcy is filed. There is no requirement Shumate use any of the funds from the CFC Plan for retirement; he can do with them as he pleases. It seems unlikely Congress would have drawn ERISA to protect retirement, craft the Bankruptcy Code as all inclusive of a debtor's property, but yet allow a debtor like Shumate to control and direct a large retirement fund which he could exempt from creditors and then use upon termination as he so chooses.

CONCLUSION

The central question of whether "applicable nonbankruptcy law" in 11 USC §541(c)(2) is meant to include ERISA or is

a state spendthrift trust determination is clearly an important question of federal law which has not been, but certainly should be, settled by this Court. It is equally important to determine the related federal law question as to whether ERISA, in and of itself, creates an exemption in bankruptcy under 11 USC §522(b). Both questions represent issues which should reflect a uniform federal law for two subject matters which are exclusively federal in their operation: the Bankruptcy Code and ERISA.

The national confusion over this area of Bankruptcy Code and ERISA conflict has created diametrically opposed applications of federal law which places bankruptcy trustees, debtors, and retirement plans in all Circuits in persistent litigation over an area which should be settled by this Court. The inconsistent and unequal

application of the Bankruptcy Code and ERISA created by the conflicting decisions of the Courts of Appeal should be resolved as soon as possible. Previously, the Court denied certiorari in Daniel, 106 S.Ct. 1199, and Lucas, 111 S.Ct. 2275; two decisions involving the issues represented by this case which reach absolutely contrary results. Until the Supreme Court acts to resolve the issues raised by this case, this important area of federal law will remain a quagmire of conflict, forum shopping and uncertain liability for thousands of parties involved in bankruptcy or ERISA matters, all of whom should be able to rely on a uniform interpretation of federal law.

The Shumate case represents a clear opportunity for the Supreme Court to resolve these conflicts by granting this Petition for a Writ of Certiorari.

Respectfully submitted,

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APPENDIX

PUBLISHED
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

Joseph B. Shumate Jr., Plaintiff-Appellant, v. John R. Patterson, Trustee, Defendant-Appellee, and ROY V. CREASY; COLEMAN FURNITURE CORPORATION, PENSION PLAN, Defendants.	No. 88-2174

Appeal from the United States
District Court
for the Western District of Virginia
at Roanoke.
Glen M. Williams, Senior District Judge.
(CA-86-272)

Argued: April 10, 1991

Decided: August 12, 1991

Before PHILLIPS and SPROUSE,
Circuit Judges,
BUTZNER, Senior Circuit Judge.

Reversed by published opinion. Judge Phillips wrote the opinion, in which Judge Sprouse and Senior Judge Butzner joined.

COUNSEL

ARGUED: Robert Arnold Lefkowitz, MALONEY, YEATTS & BARR, P.C., Richmond, Virginia; Joseph B. Shumate, Jr., Pulaski, Virginia, for Appellant. George Steven Agee, OSTERHOUDT, FERGUSON, NATT, AHERON & AGEE, P.C., Roanoke, Virginia, for Appellee. ON BRIEF: Kevin R. Huennekens, MALONEY, YEATTS & BARR, P.C., Richmond, Virginia, for Appellant.

OPINION

PHILLIPS, Circuit Judge:

This appeal requires us to revisit the question whether an interest in an ERISA-qualified pension plan (a trust) should be included as property of the debtor's estate, where the self-settled trust contains an ERISA-imposed non-alienation provision but otherwise would not qualify as a spendthrift trust under state law. We hold that under *In re Moore*, 907 F.2d 1476 (4th Cir. 1990), the interest here in issue is not includible in the debtor's estate

and accordingly reverse the district court's holding to the contrary.

I

Joseph Shumate was the president and chairman of the board of Coleman Furniture Co. ("Coleman") from 1978 until early 1983. During this time, he controlled 96% of the voting stock and had the power to appoint and control the board of directors. Both before and after Shumate joined the company, Coleman had an ERISA-qualified pension plan that was financed solely by employer contributions. Shumate had an interest in the pension plan valued at $250,000; nearly 400 other Coleman employees also participated in the plan, though to a far lesser extent.

In 1982, Coleman suffered financial problems, and filed for bankruptcy protection. Shortly thereafter, Shumate experienced financial difficulties himself,

and he filed for bankruptcy in June 1984. John R. Patterson, the defendant in this lawsuit, was appointed a trustee for Shumate's bankruptcy estate. After much litigation over the Coleman pension plan, all of the 400 Coleman workers except Shumate were paid off in full by Coleman's bankruptcy estate. As a result, Patterson filed an adversary proceeding in bankruptcy court against Coleman's trustee to recover Shumate's interest in the pension plan so it would be included in Shumate's bankruptcy estate. Shumate responded by asking the district court, engaged in a related proceeding, to compel Coleman's trustee to pay directly to him his interest in the plan. The district court assumed jurisdiction over the bankruptcy court action and granted Patterson leave to intervene.

The court then held that Shumate's

interest in the plan should be included in the estate, pursuant to 11 U.S.C. §541(a), on the basis that Shumate's control over the pension plan was so complete as not to qualify the pension plan, under applicable Virginia law, for spendthrift trust status. The court further held that assuming Shumate's interest in the pension was deemed property of the estate, it was not exempted by virtue of §522(b)(2)(A), because Shumate's interest in the ERISA-qualified pension plan was not "exempt under federal law."

This appeal by Shumate followed.

II

Section 541 of the Bankruptcy Code provides that "all legal or equitable interests of the debtor in property as of the commencement of the case" become part of the bankruptcy estate. Though this provision was intended to be broad in

scope, *see United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204-05 (1983); H.R. Rep. No. 595, 95th Cong., 1st Sess. 367-38, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 6323-24, the Code allows certain exceptions. 11 U.S.C. §541(a)(1). One of the exceptions stipulates that "[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under *applicable nonbankruptcy law* is enforceable in a case under [the Bankruptcy Code]." *Id.* §541(c)(2) (emphasis added).

After the district court's decision in the instant case, this court held in *Anderson v. Raine (In re Moore)*, 907 F.2d 1476 (4th Cir. 1990), that "applicable nonbankruptcy law" includes the Employment

Retirement Insurance Security Act (ERISA).[1] In that case we looked to the plain language of the statute and found "applicable nonbankruptcy law" to be not limited to state law but also to embrace federal statutes, including ERISA. 907 F.2d at 1477-79 ("'Applicable nonbankruptcy law' means precisely what it says: all laws, state and federal, under which a transfer restriction is enforceable. Nothing in the

[1]Other courts have interpreted "applicable nonbankruptcy law" to refer only to state spendthrift trust laws. *See, e.g., In re Goff*, 706 F.2d 574 (5th Cir. 1983); *see also In re Daniel*, 771 F.2d 1352 (9th Cir. 1985) (following *Goff*); *In re Lichstrahl*, 750 F.2d 1488 (11th Cir. 1985) (same); *In re Graham*, 726 F.2d 574 (5th Cir. 1983) (same). On that basis, those courts have declined to consider ERISA an "applicable nonbankruptcy law" so as to exclude pension plan interests from a bankruptcy estate. For the reasons set forth in *In re Moore*, 907 F.2d 1476, we disagree. *Accord In re Lucas*, 924 F.2d 597 (6th Cir. 1991) (following *Moore*); *In re Kincaid*, 917 F.2d 1162, 1169-70 (9th Cir. 1990) (Fletcher, J., concurring) (concluding that *Daniel* was wrongly decided and urging that *Moore* be followed).

phrase 'applicable nonbankruptcy law'... suggests that the phrase refers exclusively to state law much less to state spendthrift trust law."). We further held that because ERISA enforces restrictions on the transfer of pension interests under its non-alienation requirement,[2] it constitutes an

[2]In order to gain tax-exempt status, every plan must contain a non-alienation provision. *See* 26 U.S.C. §401(a)(13) ("benefits provided under the [qualified trust] plan may not be assigned or alienated"); *see also* Treas. Reg. §1.403(a)-13(b)(1)("[A] trust will not be qualified unless the plan of which the trust is a part provides that benefits provided under the plan may not be anticipated, assigned (either at law or in equity), alienated or subject to attachment, garnishment, levy, execution or other legal or equitable process."). Appellees suggest, relying on the Fifth Circuit opinion in *Goff*, that because this requirement is imposed through the tax laws and is not an affirmative law, the requirement has less force. Aside from the unassailable point that many things are accomplished through tax laws that, for one reason or another, are not done through affirmative laws, this suggestion also ignores case law, which has enforced the non-alienation provision in a number of ERISA plans. *See, e.g., Tenneco Inc. v.*

"applicable nonbankruptcy law." *See id.* at 1479-81.

Under the *Moore* analysis, therefore, the ERISA non-alienation requirement qualifies as "[a] restriction on the transfer of a beneficial interest of the debtor in a trust enforceable under applicable nonbankruptcy law." Appellees concede as much, but seek to escape the force of *Moore* by contending that *Moore* does not stand for an ironclad proposition that ERISA creates an automatic exclusion in bankruptcy, but that such an exclusion must turn on "state law governing spendthrift trust or public policy." We disagree.

First Virginia Bank, 698 F.2d 688 (4th Circ. 1983) (a debtor's interest in a qualified ERISA plan held exempt from a third party creditor's garnishment, based on the non-alienation provision). However imposed, the non-alienation provision has teeth.

The nub of appellees' argument is that the non-alienation requirement in Coleman's ERISA-qualified pension plan did not effectively apply to Shumate because he controlled the company and thereby could control the pension plan.[3] The evidence is that Shumate held 96% of the stock of the company, that he could vote in or out all the board of directors, that the board could terminate the pension plan at any time, and that he would personally benefit from any reversion from the plan upon termination. From this the district court concluded that a trust in which a beneficiary wields such power cannot be held a valid spendthrift trust, since public policy dictates that when debtor is both settlor and beneficiary of the trust

[3]Shumate's level of *potential* control is great and not seriously disputed, though Shumate contends that his legal and actual control is small.

it will not be enforced.

This focus on state spendthrift trust law, which looks to the reality behind the non-alienation provision, is misplaced. ERISA requires a plan to have a non-alienation provision, and that provision has been vigorously enforced. *See Guidry v. Sheet Metal Workers Nat'l Pension Fund*, 110 S. Ct. 680 (1990); *Smith v. Mirman*, 749 F.2d 181, 183 (4th Cir. 1984); *General Motors Corp. v. Buha*, 623 F.2d 455, 460 (6th Cir. 1980). No more inquiry need be made to determine whether the trust is controlled by the settlor or the beneficiary or whether they are the same person. As we held in *Moore*, "ERISA's non-alienability provisions prevent both voluntary and involuntary encroachments on vested benefits. Thus, neither plan participants nor general creditors may reach benefits under an ERISA-qualified

profitsharing and pension fund." 907 F.2d at 1480 (citations omitted). Looking only to the terms of the plan before us, we are satisfied that this conclusion also applies to the Coleman pension plan.

Hence, this court's holding in *Moore* precludes the fact-based state law inquiry urged by appellees. We think it is not giving *Moore* undue weight to say that it stands for the proposition that all ERISA-qualified plans, which by definition have a non-alienation- provision, constitute "applicable nonbankruptcy law" and contain enforceable restrictions on the transfer of pension interests. *Id.* That conclusion rests not on the reality of the particular beneficiary-settlor-trust relationship in issue, but instead on the status of the plan as ERISA qualified. Consequently, Shumate's interest in the pension plan should be excluded from the bankruptcy

estate under §541(c)(2).[4]

This holding is consistent with the clear intent of ERISA and the Bankruptcy Code. Congress passed ERISA to guarantee that "if a worker has been promised a defined pension benefit upon retirement - and if he has fulfilled whatever conditions are required to obtain a vested benefit-he actually will receive it." *Nachman Corp. v. Pension Benefit Guaranty Corp.*, 446 U.S.359,375 (1980). To make sure this guarantee was not eroded, Congress imposed restrictions on the assignment and

[4]Creditors concerned that a non-alienation provision is ineffective because of a debtor's control over a pension plan, either before or after bankruptcy, are not without other means of protection. Under 11 U.S.C. § 548, a bankruptcy estate trustee can void a debtor's transfer of property that was made in the prior twelve months and was made with the intent to hinder, delay, or defraud creditors. In this way, creditors can block a debtor in Shumate's position from actually taking advantage of his control position and depleting the estate.

alienation of pension benefits. *See* 29 U.S.C. § 1056(d)(1); 26 U.S.C. § 401(a)(13). These restrictions demonstrate a "strong public policy against the alienability of an ERISA plan participant's benefits." *Smith v. Mirman*, 749 F.2d at 183. The strength of this public policy judgment was reaffirmed recently by the Supreme Court in *Guidry v. Sheet Metal Workers Nat'l Pension Fund*, 110 S. Ct.680 (1990). In *Guidry*, the Court held that the pension fund could not attach Guidry's pension benefits to recover the money Guidry had embezzled from the fund. The Court held that ERISA's nonalienation requirement "reflects a considered congressional policy choice, a decision to safeguard a stream of income for pensioners (and their dependents...), even if that decision prevents others from securing relief for the wrongs done them." 110 S. Ct. at 687.

The Bankruptcy Code reflects a different, but not incompatible, congressional intent. In enacting the Code, Congress sought to define broadly a debtor's estate, *Whiting Pools*, 462 U.S. at 204, but also recognized that certain property should be excluded from the estate. *See* 11 U.S.C. § 541 (b), (c)(2). One class of property universally recognized as not included is a debtor's interest in a spendthrift trust. *See, e.g.*, *McLean v. Central States, Southeast & Southwest Areas Pension Fund*, 762 F.2d 1204 (4th Cir. 1985); *Goff*, 706 F.2d 574. Courts have so held because § 541 mandates that where trusts contain enforceable restrictions on transfer of a beneficial interest, those restrictions must be recognized in bankruptcy and there operate to exclude the interest from the debtor's estate. As this court made clear in *Moore*,

we see no reason to restrict § 541(c)(2)'s exclusion provision to spendthrift trusts. Instead, following the rule that, whenever possible, statutes should be read in harmony and not in conflict, *Morton v. Mancari*, 417 U.S. 535, 551 (1974), we interpret these in such a way as to give full effect to both ERISA and the Bankruptcy Code by holding that interests in ERISA-qualified pension plans are excluded from a bankrupt's estate. *See Moore*, 907 F.2d at 1479-80.

III

Because we hold that debtor's interest in the pension plan is excluded from the estate, we need not reach the question whether debtor's interest would in any event qualify for exemption under § 522(b). *See* 11 U.S.C. § 522(b) ("an individual debtor may exempt from property of the estate... any property that is exempt under

Federal law").[5] Accordingly, the judgment of the district court is reversed.

REVERSED

[5]For a persuasive opinion that such an interest should, under § 522, be subject to exemption because ERISA is "federal law," *see In re Komet*, 104 B.R. 799 (Bankr. W.D. Tex. 1989).

Roy V. CREASY, Trustee in Bankruptcy for Coleman Furniture Company, Plaintiff,

v.

COLEMAN FURNITURE CORPORATION, Defendant.

Civ. A. No. 86-0272-R.

United States District Court, W.D. Virginia, Roanoke Division.

March 1, 1988.

Chapter 7 debtor sought turnover of his interest in his bankrupt firm's pension plan. The District Court, Glen M. Williams, J., found that: (1) debtor who exercised complete control over his firm's pension plan could not exclude his interest in claim from his Chapter 7 bankruptcy estate, and (2) debtor could not exempt his interest in plan.

Ordered accordingly.

1. Bankruptcy 2548

Debtor's interest in his firm's pension plan was includable in his bankruptcy estate, though plan purported to be spendthrift trust, in that debtor exercised complete control over firm, and thus had authority to terminate plan at will and pay proceeds to himself; fact that debtor signed loan agreement which prohibited removal of collateral from firm did not change legal control debtor exercised over pension plan. Bankr.Code, 11 U.S.C.A. § 541(c)(2).

2. Bankruptcy 2779

Chapter 7 debtor's interest in pension plan was not exempt, though plan contained clause prohibiting assignment to creditors. Bankr.Code, 11 U.S.C.A. § 522(b)(2)(A).

Roy V. Creasy, Roanoke, Va., Trustee for plaintiff.

Harry S. Rhodes, Roanoke, Va., for plaintiff.

James F. Douthat, Roanoke, Va., George V. Hanna, III, Charlotte, N.C., Joseph B. Shumate, Jr., Pulaski, Va., William M. Mercer-Meidinger, Inc., Richmond, Va., for defendant.

MEMORANDUM OPINION

GLEN M. WILLIAMS, District Judge.

The principal question presented in this case is whether a debtor who exercised complete control over his firm's pension plan may exclude his interest in the Plan from his Chapter 7 bankruptcy estate under the "non-bankruptcy law" exclusion of 11 U.S.C. § 541(c)(2) or the "federal law" exemption of § 522(b)(2)(A). The court rules that he cannot and denies the debtor's motion to compel the firm's Chapter 7 trustee to pay him his pension interest.

I. PROCEDURAL HISTORY AND FINDINGS OF FACT

These proceedings revolve around the Coleman Furniture Corporation (CFC), a Virginia corporation, and its president and majority stockholder, Joseph B. Shumate, Jr. (Shumate), a Virginia resident, both of whom are undergoing liquidation pursuant to Chapter 7 of the bankruptcy code. *See also Creasy v. Coleman Furniture Corp.*, 763 F.2d 656 (4th Cir.1985), Roy V. Creasy (Creasy), as Chapter 7 trustee for CFC, originally petitioned this court to employ actuaries to terminate the CFC plan in an adversary proceeding against CFC. Shumate, as a *pro se* intervenor, filed a motion to compel Creasy to pay him his benefits under the plan. John R. Patterson, Shumate's Chapter 7 trustee, was permitted to intervene because he also claimed ownership of Shumate's interest in the pension plan.

Although Shumate also had contested the trustee's calculation of his interest in the plan, he and the trustees have agreed to settle that portion of the dispute.[1] Therefore, the only issue before the court is whether to grant Shumate's motion to compel.

The CFC pension plan was created in 1964. Although the original fund documents have been amended and restated since that time, the parties have stipulated that the 1976 pension fund plan documents (plan)

[1]. Shumate originally calculated his interest in the plan to be $300,000 while the plan's trustee's figure was closer to $200,000. This dispute over the amount was settled by requiring the trustee to deposit $250,000 in escrow to satisfy Shumate's pension claim. This allowed the plan to settle with all other pension participants. In return for this settlement, Shumate agreed to drop his claims against the trustee for breach of fiduciary duty. Once the right to Shumate's interest is settled and final expenses are paid, approximately $561,000 will revert to Creasy as CFC's bankruptcy trustee.

govern this case. The plan provides that CFC can terminate the pension fund at any time. Upon termination, the plan allowed a recipient to receive a lump fund payment instead of a life annuity. Shumate has had voting control of CFC from at least 1978 through his ownership of CFC stock and the right to vote other stock held in a voting trust. Therefore, Shumate could have terminated the plan at any time before the bankruptcy and received not only his pension interest, but any excess funds not needed to satisfy the rights of other participants. To date, all participants have made some payment arrangement with the pension except for Shumate. The plan prohibits the alienation of benefits or the transfer of plan assets for the benefit of creditors, as required by 29 U.S.C. § 1056(d)(1) (Employee Retirement Income Security Act (ERISA)) and 26 U.S.C. §

401(a)(13) (Internal Revenue Code).

CONCLUSIONS OF LAW

Conceptually, the task at hand is easily grasped. Once a debtor files a petition in bankruptcy under Chapter 7, an estate is created. 11 U.S.C. § 541(a) (1985). The estate is comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case." *Id.* Notwithstanding these broad provisions, a debtor may exclude certain specifically enumerated assets from the liquidation process. § 522(b). This statutory framework reveals that there are two decision points crucial to Shumate's recovery of his interest in the pension plan. First, the asset must not be included in his liquidation estate. Second, if the asset is part of the estate, he must place it within one of the exclusions. Otherwise, Shumate must

deliver the asset to the trustee, § 521(4), who in turn must reduce the property to money in order to settle the claims of all creditors. § 704(1). The court begins first with the issue of whether the pension is part of Shumate's Chapter 7 estate.

Whether Shumate May Exclude His Interest From the Chapter 7 Estate through § 541(c)(2)

The bankruptcy code includes "all legal and equitable interests" in the bankrupt's estate except as specifically excluded. § 541(a). There is no doubt that a bankrupt's interest in a pension plan is a legal or equitable interest; this conclusion flows from the sweeping language and the accompanying legislative history. *See McLean v. Cent. States, S. & S. Areas Pen. Fund,* 762 F.2d 1204, 1206 (4th Cir. 1985). The analysis must therefore focus on the statutory exclusions from the

estate.

The only exclusion applicable to Shumate's interest in the CFC pension plan is found in § 541(c)(2) of the code: "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title." The Fourth Circuit has interpreted the phrase "nonbankruptcy law" to mean state law. *See McLean, 762 F.2d at 1207-06* (Illinois law controlled to apply § 541(c)(2)). The question then becomes whether the CFC pension trust is a valid spendthrift trust under Virginia law, which governs the plan.

Virginia recognizes spendthrift trusts. Va.Code § 55-19 (1986).[2] To be

[2]. **Estates in trust subject to debts of beneficiaries; exception for spendthrift trusts.--** Estates of every kind holden or possessed in trust shall be subject to the

valid a trust must have "a competent settlor and trustee, an ascertainable trust res and certain beneficiaries." *In re Wilson*, 3 B.R. 439, 442 (Bankr.W.D.Va.1980). The CFC pension plan seems to satisfy these requirements: Article VII of the plan provides for the creation of a trust fund in accordance with a trust agreement incorporated by reference in the plan; Article II defines the beneficiaries as eligible CFC employees, Article VII provides for the funding of the

debts and charges of the persons to whose use or to whose benefit they are holden or possessed, as they would be if those persons owned the list interest in the things holden or possessed as in the uses or trusts thereof; but any such estate, not exceeding $500,000 in actual value, may be holden or possessed in trust upon condition that the corpus thereof and income therefrom, or either of them, shall be applied by the trustee to the support and maintenance of the beneficiaries without being subject to their liabilities or to alienation by them, but no such trust shall operate to the prejudice of any existing creditor of the creator of such trust.

trust res held by the bank; the trust purpose is legal as it is a private pension plan; and Article XII contains a non-assignability provision.[3] *Cf. Parkinson v. Bradford Trust Co. of Boston (In re O'Brien)*, 50 B.R. 67 (Bankr.E.D.Va.1985) (Keogh Pension Trust valid under Virginia law but spendthrift provision unenforceable because of settlor-beneficiary relationship).

However, the significant issue in this case is whether the court should deny Shumate his interest in the trust on the authority of a long line of cases which invalidate pension trusts vis-a-vis the debtor for public policy reasons when that debtor is both the settlor and beneficiary

[3]. The court does not address the $500,000 limitation provided by § 55-19 but assumes, *arguendo*, that there is no problem since only the $250,000 remaining in the plan is at issue and all other claims have been satisfied.

of the trust. *E.g., Matter of Goff*, 706 F.2d 574 (5th Cir. 1983). The Fourth Circuit has adopted this precedent in *McLean* where it is stated: "Moreover, the [pension fund in this case] is not one of those which because settled and revocable by a beneficiary, may not on that account for public policy reasons be protected against the claims of the beneficiary's creditors by anti-assignment provisions." 762 F.2d at 1207. The court later restated its adoption of the doctrine citing *Goff*. *Id.* at 1208. Therefore, the court rejects the cases Shumate has cited which did not accept the doctrine, *e.g., In re Ralstin*, 61 B.R. 502 (Bankr.D.Kan. 1986), but reviews other cases to determine the doctrine's parameters and whether this case falls within its purview.

The Fifth Circuit in *Goff* seems to have been the first to best articulate the

policy. In *Goff* the court stated that the ERISA-qualified Keogh plan at issue could not be viewed as a spendthrift trust because the self-employed "settlors" had created what was in effect a revocable trust for their own benefit. *Id.* at 580-82. The court believed the provision applied to "traditional spendthrift trusts," *Id.* at 581, a limitation to the language specifically rejected by the Fourth Circuit. *McLean*, 762 F.2d at 1207 n. 1. Other courts have invalidated pension trusts vis-a-vis the debtor in the settlor-sole beneficiary context. *See In re Daniel,* 771 F.2d 1352 (9th Cir.1985) and *In re Graham,* 726 F.2d 1268 (8th Cir.1984) both of which involved physicians who were settlors/sole beneficiaries/trustees of their professional corporation's ERISA-qualified pension plans. This case presents different facts because Shumate

was not the settlor of the plan, he was one of approximately 400 beneficiaries, and CFC is not a small professional corporation.

The trustee argues that the doctrine extends to the facts of this case because of the control Shumate exercised over CFC. The trustee points to *In re Lichstrahl*, 750 F.2d 1488 (11th Cir.1985) which involves an M.D.-controlled professional corporation with an ERISA-qualified pension plan. The court held the spendthrift trust was not valid under Florida law because the physician, the plan's major beneficiary, could control disbursements from the plan through his power of revocation. 750 F.2d at 1490. Under Florida law, this control rendered the trust invalid as such trusts were meant to protect the beneficiary not only from his creditors, but from himself. *See Croom v. Ocala Plumbing & Electric Co.*, 62 Fla. 450, 57 So. 243 (1911); *see also*

Nixon v. P.J. Pedone & Co. (In re Nichols), 42 B.R. 772, 776 (Bankr.M.D.Fla.1984). Although *Lichstrahl's* facts involve a settlor-beneficiary relationship, the case is significant for recognizing the element of control as a bar to enforcing a spendthrift provision in the bankruptcy context. At least one court has provided a good explanation of the control test:

> The degree of control that the debtor may exercise over the trust assets is a crucial factor in determining the issue of inclusion in, or exclusion from, the bankruptcy estate. If the debtor's access to the funds is relatively unfettered, exclusion from the bankruptcy estate would create a temptation to shelter assets in a trust and withdraw them for personal use upon issuance of the bankruptcy discharge. *Matter of Goff*, 706 F.2d at 588. Limited control may be permitted if its exercise

> would create such hardship for the debtor as to discourage its exercise except in dire circumstances. *See Matter of Baviello*, 12 B.R. 412, 415 (Bankr. E.D.N.Y.1979); *In re Wright*, 39 B.R. 623 (D.S.C.1983). Where the use of the funds would require that the debtor leave employment, become disabled or die it is clear that the funds retain their nature as future earnings rather than present savings. Such provisions should not invalidate an otherwise valid spendthrift trust.

In re Pettit, 61 B.R. 341, 346 (Bankr.W.D. Wash.1986).

Courts which have applied the control test have found for and against the debtor. One court invalidated spendthrift provisions when the debtor could obtain the funds he contributed to the plan by showing an immediate and severe hardship which was

nothing more than a "mere formality." *In re Monahan*, 68 B.R. 997 (Bankr.S.D.Fla.1982). The debtor was found to possess too much control when the employer could completely or partially terminate the plan at any time for beneficiary/employees who were also sole stockholders, directors and officers of the employer. *In re Gillett*, 46 B.R. 642 (Bankr.S.D.Fla.1985). However, a debtor did not have too much control over the trust when he had to quit his job to get his money. *Gennet v. ICMA Retirement Corp. (In re Forbes)*, 65 B.R. 58 (Bankr.S.D.Fla.1986).

The *Goff* line of cases has been adopted in Virginia. *See In re O'Brien* 50 B.R. 67. *O'Brien* involved a physician who established a Keogh plan with her husband as trustee and herself as the beneficiary. The court ruled that her power to revoke

the plan at will was inconsistent with Virginia spendthrift trusts law. 50 B.R. at 77. *O'Brien* was concerned with the strong public policy against allowing someone to place his own property in a spendthrift trust to the detriment of creditors. *Id.* at 74. The court found authority for this policy in *Petty v. Moores Brook Sanitarium,* 110 Va. 815, 67 S.E. 355 (1910) which arose prior to the Virginia spendthrift trust statute but was overruled only to the extent of allowing spendthrift trusts, not for the proposition that a settlor cannot be the beneficiary of his own spendthrift trust. 50 B.R. at 75-76.

This court believes the control test is applicable under Virginia law to determine how much power a beneficiary can exercise over a spendthrift trust before a court will invalidate it. Although there

are no Virginia cases on point, as a matter of trust theory, it seems inconsistent that a beneficiary can revoke at will his own spendthrift trust. After all, a spendthrift trust is designed not only to protect the beneficiary from his creditors but from himself. *See In re Wilson*, 3 B.R. 439, 444 (Bkrtcy.W.D.Va.1980). Furthermore, this doctrine is a matter of public policy. *McLean*, 762 F.2d at 1207; O'Brien, 50 B.R. at 74. The Virginia Supreme Court was very much concerned with public policy when it interpreted the spendthrift statute in *Sheridan v. Krause*, 161 Va. 873, 172 S.E. 508 (1934). Public policy demands that debtors not be allowed access to their funds to the detriment of creditors in appropriate cases. 50 B.R. at 74.

[1] The facts reveal that Shumate exercised great control over the CFC plan.

Before the bankruptcy, he had voting control of the stock and could have voted it to terminate the plan at any time. Upon termination, he, as a plan participant, had the choice of a lump sum payment. He also could have paid himself the reversion of any overfunded amount as a dividend on his stock. Therefore, Shumate's right to the trust assets went far beyond the hardship provisions ERISA allows beneficiaries to have in qualified plans. *See* 29 U.S.C. § 1056. Some courts have held that, although originally not the settlor of the ERISA qualified spendthrift trust, someone who holds such a power of revocation is deemed as a matter of law to be the settlor thereby falling within the *Goff* doctrine. *See, e.g. Hunter v. Ohio Citizens Bank (In re Hotchkiss,* 75 B.R. 115 (Bankr.N.D.Ohio 1987) (although the debtor was only the corporate secretary when the plan was

formed, his status as officer and shareholder makes him a settler of the pension trust). Shumate exercised such power over the CFC pension trust that he could control it to suit his needs. Such dominion is inconsistent with the notion of spendthrift trusts.

Shumate argues that he did not control the trust for two reasons. First, he argues he could not terminate the pension plan and pay out the proceeds because he was prohibited from doing so by the terms of a loan agreement he signed with North Carolina National Bank Financial Services (NCNB-FS). This agreement prohibited the removal of collateral from the business or the payment of a dividend over $50,000.[4]

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[4]. ARTICLE III

Security

3.04 The collateral referred to in Section 3.01(a) shall be used for the purpose intended by its purchase in the business of the Company. The Company agrees that such collateral will not be misused or abused, wasted or allowed to deteriorate, except in the ordinary wear and tear of its intended use.

ARTICLE VI

Negative Covenants

6.01 Until payment in full of the principal and interest of the Note and all of its obligations under the Financing and Security Agreement, the Company covenants that it will not, nor will it enter into any binding agreement to (without the prior written consent of the Lender):

* * * * * *

(h) declare or pay any dividends for any fiscal year on any class of its stock of more than Fifty Thousand Dollars ($50,000.00) in the aggregate other than dividends payable solely in shares of common stock or make any other distribution to any shareholder as such; provided, however, before any dividend payment, after tax profits must exceed debt service by Fifty Thousand Dollars ($50,000.00) for such fiscal year.

Loan Agreement of January 4, 1978 signed by J. B. Shumate.

These facts do not change the legal control Shumate exercised over the trust. The

trust instrument and any referenced documents control his powers, not the contracts signed with the bank. *See 19 Michie's Jurisprudence, Trusts and Trustees,* § 87 (1979). He could still terminate the pension plan and pay the proceeds out as a dividend. Although the consequences of these acts include acceleration of the note and liability for breach of contract, he nonetheless had legal control over the pension plan. Shumate surrendered the control for consideration, namely, the amount of the loan. Therefore, Shumate obtained benefits from rights he had as majority stockholder in control of the corporation. Even if the contract did change the legal right to control the trust, this court believes Shumate would be estopped from asserting an act of his own will as a bar to an exercise of power he lawfully possessed. *See* Restatement of

(Second) Agency § 8B (1934).

The second argument Shumate makes for why he did not have control over CFC is that his power over the corporation was wrested away from him by his and CFC's bankruptcies. This argument also fails. The control at issue is that which Shumate exercised *prior* to CFC's November 3, 1982 bankruptcy filing. Even after a Chapter 11 application, Shumate was a debtor-in-possession with all the powers of a trustee. *See* 11 U.S.C. § 1107(a). It was not until the conversion to Chapter 7 in July of 1983 that Shumate lost control of CFC to the Chapter 7 trustee. *See Id.* § 521(3). The loss of control due to the extraordinary event of liquidation does not affect his prior control of CFC from at least 1978.

Whether Shumate's Interest in the CFC Plan May be Exempted Under

§ 522(b)(2)(A)

[2] Once a court has decided an asset is part of the bankruptcy estate, the next step in the analysis is to decide whether the asset may be exempted. At first glance, § 522(d)(10)(E), which exempts pensions, would grant Shumate the relief he seeks. However, § 522(b)(1) allows the states to preclude debtors from claiming the § 522(d) exemptions. Virginia has elected to opt out of these exemptions through § 34-31. *In re Calhoun*, 47 B.R. 119 (Bankr.E.D.Va.1985); *See generally*, J. Reynolds, *How Bankruptcy Exemptions Work: Virginia as an Illustration of Why the "Opt out" Clause Was a Bad Idea,* 8 GMU L.Rev. 1 (1985).

The only remaining exclusion that might apply is found in § 522(b)(2)(A) which exempts any estate property that is

exempt under "Federal law."[5] The argument goes as follows: Since the pension plan contains an anti-assignment clause as required by ERISA's 29 U.S.C. § 1056(d)(1) and IRC's 26 U.S.C. § 401(a)(13), Shumate's interest is "exempt under federal law" from the bankruptcy estate.

Only a few courts have accepted the argument. *See, e.g., In re Hinshaw*, 23 B.R. 233 (Bankr.D.Kan.1982). The weight of

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[5]. The relevant portions read as follows:

(b) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (1) or, in the alternative, paragraph (2) of this subsection.

* * * * * * *

(2)(A) Any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180-day period than in any other place; and . . . .

authority is to the contrary. *Goff* 706 F.2d at 589; *Lichstrahl*, 750 F.2d at 1488; *Graham*, 726 F.2d 1268; *Daniel*, 771 F.2d at 1360-61. ERISA-qualified pension plans do not fall within § 522(b)(2)(A) for at least two reasons. First, the House and Senate reports contain a list of property that can be exempted under federal laws and ERISA is conspicuously absent. *See, e.g.* S.Rep. No. 989, 95th Cong., 2d Sess. 75, *reprinted in* 1978 U.S.Code Cong. & Ad. News 5787, 5861. Second, the exempted property relates to "pensions, wages, benefits and payments (which) are all peculiarly federal in nature, created by federal law or related to industries traditionally protected by the federal government. In sharp contrast, ERISA regulates private employer pension systems." *Lichstrahl*, 750 F.2d at 1491 *quoting Graham*, 726 F.2d at 1274. This court adopts the reasoning of the circuit

courts which have ruled on the issue and rejects the *Hinshaw* analysis.

CONCLUSION

The motion to compel CFC's Chapter 7 trustee and plan administrator to pay Shumate his interest in the pension plan is DENIED. First, Shumate may not exclude his interest because the plan qualifies as a spendthrift trust. The control he exercised over the plan is inconsistent with the notion of a spendthrift trust. Furthermore, public policy would be violated if he could deny his creditors access to funds which were essentially a personal savings account. Second, Shumate may not exempt his interest because the plan is ERISA-qualified. Neither the legislative history nor the cases which have analyzed this issue indicate Congress intended to exempt private pension plans from the bankruptcy estate.

The Clerk is directed to send certified copies of this Memorandum Opinion to counsel of record.

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
ROANOKE DIVISION

ROY V. CREASY, Trustee in Bankruptcy for Coleman Furniture Company	) CIVIL ACTION No. 86-0272-R
v.	)
COLEMAN FURNITURE CORPORATION	) MEMORANDUM OPINION

This case is before the court on a motion to reconsider and amend filed by Joseph B. Shumate, Jr., (Shumate) intervenor, pursuant to Fed. R. Civ. P. 52(b). Shumate seeks an amendment to an order entered February 29, 1988 which denied his motion to compel Roy V. Creasy, (Creasy) trustee in Bankruptcy for Coleman Furniture Company, (CFC) to pay him his interest in the CFC pension plan. Shumate advances the following principal grounds as justification for granting the motion to compel; (1) the cases relied on by the court are not factually similar to the case

as bar; (2) the ruling jeopardizes the status of other beneficiaries; (3) the order contains "factual errors and misconceptions," and, (4) he has already elected to receive a pension. Each ground is addressed in turn.

Control Test

Shumate argues that the cases relied on by the court involve self employment retirement plans and not defined benefit non-contributory plans as is the CFC plan. The court recognized the extent of some of the factual distinctions for the leading cases at page 6 of its opinion. "This case presents different facts because Shumate was not the settlor of the plan, he was one of approximately 400 beneficiaries, and CFC is not a small professional corporation." Regardless, the facts of the individual cases were not controlling; it was the language and reasoning articulated in those

cases which persuaded the court. The control test seems to be so widely accepted that textbooks have adopted it as blackletter law. See 60A Am Jur 2d, Pensions and Retirement Funds §474 (1988) where the author states: "[a] retirement plan does not qualify as a spendthrift trust if a debtor has any means to gain access to plan funds when bankruptcy is filed and a bankruptcy estate is created."

Plan as Spendthrift Trust

Shumate argues that the court jeopardizes the retirement of all other CFC participants in its ruling. This is not true. The court ruled, arguendo, that the plan qualified under §55-19; but, it also ruled that for Shumate alone the spendthrift trust clause would not be upheld under the nonbankruptcy law exclusion of 11 U.S.C. §541(c)(2)(1984). The status of the trust vis-a-vis other

participants was not at issue.

Factual Errors and Misconceptions

Shumate argues that numerous factual errors and misconceptions pervade the opinion. He recites a lengthy chronological history of events surrounding his employment with CFC which was not before the court. The court took the facts from the briefs and the stipulations contained in the record. Nothing appears at odds with the most critical fact in the case, viz: through control over a majority of CFC stock, Shumate controlled the corporation and its affairs, including the pension plan.

Prior Election to Receive Pension

Finally, Shumate argues"

> [he] elected to take his pension as a lifetime annuity beginning on March 1, 1983 after he was terminated by Coleman pursuant to the plan. This was

> fifteen months before Shumate took bankruptcy. Shumate's Trustee, Mr. Patterson, has no standing whatsoever to revoke a decision made more than a year before a bankruptcy was filed.

Brief at ¶34, see also Id. at ¶36.

This is the first time this argument has been made to the court. Assuming, arguendo, these facts are true, they do not affect the court's decision. Elected or not, the law will not enforce Shumate's right to the pension interest.

The court has reconsidered and finds no reason in law or fact to alter its decision. Accordingly, the order dated February 29, 1988 shall stand and the clerk shall send certified copies of this opinion to counsel of record.

ENTER: This the 13th day of April, 1988.

/s/ Glen M. Williams
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
ROANOKE DIVISION

ROY V. CREASY, TRUSTEE IN BANKRUPTCY FOR COLEMAN FURNITURE CORPORATION Plaintiff vs. COLEMAN FURNITURE CORPORATION Defendant	CIVIL ACTION NO. 86-0272-R FINAL ORDER

THIS DAY came the parties, John R. Patterson, Trustee in Bankruptcy for Joseph B. Shumate, Jr., by counsel, Roy V. Creasy as Plan Administrator of the Coleman Furniture Corporation Pension Plan and as Trustee in Bankruptcy for Coleman Furniture Corporation, by counsel, and Joseph B. Shumate, Jr., pro se, pursuant to a motion filed by John R. Patterson for an Order of Disbursement and Final Order.

Upon consideration of the Motion, the

arguments of counsel and for good cause shown, the Court finds that:

1. All matters involving Shumate's interest in the Coleman Furniture Corporation Pension Plan have been adjudicated by this Court in its orders of December 4, 1987, February 29, 1988, and April 13, 1988.

2. That Shumate and Patterson have no other interest in this matter and that those Orders are final with regard to them and with regard to any other claim regarding Shumate's interest in the Coleman Furniture Corporation Pension Plan, as regards Roy Creasy as Plan Administrator and as Trustee in bankruptcy of Coleman Furniture Corporation.

3. That Adversary Proceeding No. 7-87-0133 in the United States Bankruptcy Court for the Western District of Virginia, covers identical questions of law and fact

as determined by the Court's Orders in this matter and that it is appropriate to withdraw the reference to said Adversary Proceeding and consolidate it with this civil action.

4. That all events have occurred which now entitle Patterson as Trustee of Shumate's bankruptcy estate to be paid the funds held in the Court's registry fund representing Shumate's interest in the Coleman Furniture Corporation Pension Plan.

Therefore, it is hereby

ORDERED

1. That the Clerk of this Court pay over from the Court's registry fund those funds with accrued interest deposited therewith pursuant to this Court's Order of December 4, 1987, and representing the proceeds of Shumate's interest in the Coleman Furniture Corporation Pension Plan in the initial principal amount of

$250,000.00 plus interest accrued thereon;

2. It is further ORDERED that the reference to Adversary Proceeding No. 7-87-0133 in the United States Bankruptcy Court for the Western District of Virginia is hereby withdrawn pursuant to 28 USC §157 and such Adversary Proceeding consolidated into this Civil Action;

3. And it is further ORDERED that Shumate and Patterson are hereby dismissed as parties to this Civil Action.

4. And it is further ORDERED that Shumate's Motion for a New Trial be hereby dismissed with prejudice;

5. AND IT IS ALSO ORDERED that this ORDER is FINAL regarding Shumate's interest in the Coleman Furniture Corporation Pension Plan and regarding any and all claims by Shumate and/or Patterson against Creasy as Coleman Furniture Corporation Plan Administrator and Coleman Furniture

Corporation Trustee in Bankruptcy insofar as such claims would relate to Shumate's interest in the Coleman Furniture Corporation Pension Plan.

The Clerk of this Court shall send certified copies of this Order to counsel of record, the Clerk of the United States Bankruptcy Court for the Western District of Virginia, John R. Patterson, Trustee, Roy V. Creasy, Plan Administrator and Trustee, and to Joseph B. Shumate, Jr.

ENTER THIS 1 DAY OF September, 1988.

/s/ Glen M. Williams
JUDGE

SEEN AND AGREED TO:

John R. Patterson, Trustee

By /s/ G. Steven Agee
Of Counsel

Roy V. Creasy, Plan Administrator and Trustee in Bankruptcy

By /s/ Harry S. Rhodes
OF COUNSEL

SEEN AND OBJECTED TO:

/s/ Joseph B. Shumate, Jr., pro se

p15.ag3.p

FILED: September 13, 1991

UNITED STATES COURT OF APPEALS

FOR THE FOURTH CIRCUIT

No.88-2174

JOSEPH B. SHUMATE, JR.,

Plaintiff - Appellant,

versus

JOHN R. PATTERSON, TRUSTEE,

Defendant - Appellee,

and

ROY V. CREASY; COLEMAN FURNITURE CORPORATION, PENSION PLAN,

Defendants.

ORDER

Appellee has filed a motion to stay mandate and the appellant has filed a response in opposition to motion for stay. By order dated August 28, 1991, this Court temporarily stayed the mandate pending review of the motion and response.

The Court stays the mandate pending timely application to the United States Supreme Court for writ of certiorari. This grant of a stay of mandate is conditioned upon the requirement that the funds in question in this case shall remain on deposit with the clerk of the district court in an interest-bearing account until further order of this Court.

Entered at the direction of Judge Phillips with the concurrence of Judge Sprouse and Judge Butzner.

For the Court

/s/ John M. Greacen
CLERK

§522. Exemptions

11 USCS §522(b)(2)(A) "any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180-day period than in any other place; and"

11 USCS §541(c)(2) "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title [11 USCS §§101 et seq.]."

26 USC §401(a)(13)(A) "Assignment and alienation

(A) In general. A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that benefits provided under the plan may not be assigned or alienated. For purposes of the preceding sentence, there shall not be taken into account any voluntary and revocable assignment of not to exceed 10 percent of any benefit payment made by any participant who is receiving benefits under the plan unless the assignment or alienation is made for purposes of defraying plan administration costs. For purposes of this paragraph a loan made to a participant or beneficiary shall not be treated as an assignment or alienation if such loan is secured by the participant's accrued nonforfeitable benefit and is exempt from the tax imposed by section 4975 (relating to tax on prohibited transactions) by reason of section 4975(d)(1). This paragraph shall take effect on January 1, 1976 and shall not apply to assignments which were irrevocable on September 2, 1974."

29 USCS §1056(d)(1)

"(d) Assignment or alienation of plan benefits. (1) Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated."

29 USCS §1144(d)

"(d) Alteration, amendment, modification, invalidation, impairment, or supersedure of any law of the United States prohibited. Nothing in this title shall be construed to alter, amend, modify, invalidate, impair, or supersede any law of the United States (except as provided in sections 111 and 507(b) [29 USCS §§1031, 1137(b)]) or any rule or regulation issued under any such law."